

Decumulation – Increasing DC Plan Value And Ensuring Compliance With Best Practices (Part II)



In Part I of this series, we considered ways in which the “traditional” accumulation driven defined contribution (DC) plan design fails to maximize value. In this post, we discuss variable pensions as well as the role of governance considerations in decumulation strategies.

The interesting opportunity for plan sponsors to consider is how they might significantly increase the overall value of their DC plan through effective decumulation strategies, while doing so at an acceptable cost and without taking on an unacceptable amount of increased administration or fiduciary responsibilities as plan administrator. In this regard, there may be a number of ways to enhance DC plan value, and member appreciation of such value, without any material increase in fiduciary liability.

Payment of Variable Pensions

In many Canadian pension jurisdictions, the payment of pensions to members directly from their DC plans is either permitted, or pending the proposed introduction of enabling legislation (e.g., the federal Pension Benefits Standards Act, 1985 and recent proposals from Ontario allow (but do not require) variable payments from a member’s DC account similar to those allowed from life income funds). Where permitted, many DC plan sponsors may still think twice about adding this feature to their DC plan design, despite the value add to members, because they are concerned about prolonging pension management costs and fiduciary responsibility for the administrator beyond member retirement. However, attitudes to this may be changing along with the realization that it is possible to enhance DC plan value by the adoption of a more proactive approach to the decumulation phase of DC benefits which could, but need not, require committing the plan to directly paying pensions and which need not materially increase administration cost or fiduciary liability.

Governance/Plan Administration Considerations

CAPSA best practice guidelines for DC plans (e.g., see, in particular, Guideline No. 8 released March 28, 2014) suggest that plan administrators have a proactive role to play in assisting DC plan members to transition to the decumulation phase (even where payment of variable DC pensions are not permitted by the plan terms). While CAPSA

guidelines do not have the force of law, these guidelines may be used as a benchmark by the courts and/or regulators to assess whether a DC plan administrator has met its fiduciary obligations. As a result, it is arguable that decumulation strategies deserve serious immediate consideration as a matter of good DC governance.

CAPSA Guideline No. 8 includes discussion of the information that should be provided to members approaching the payout phase, including:

- options available to the member;
- any actions the member must take;
- any deadlines for member action;
- any default options that may be applied if no action is taken; and
- the impact that the termination of membership will have on each investment option.

In addition, the Guideline indicates that “[i]t is expected that the plan administration will provide information regarding all of the retirement products available to members with respect to the payout phase”. This information should allow members to make “informed decisions which strike a balance between protection from the risks inherent in the various products and achieving target replacement rates”.

In our next post – Part III of this series – we will consider decumulation strategies in more detail, and specific considerations for plan administrators and plan sponsors.

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Article by Ian McSweeney and Jonathan Marin